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Supreme Court, U.S.
FILED

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No. OFFICE OF THE CLERK

In The
Supreme Court of The United States
October Term 1998

SUE TOTH

Petitioner,

v.

MICHIGAN STATE HOUSING DEVELOPMENT AUTHORITY, in their official capacity; JAMES LOGUR III individually and in his official capacity; ROBERT BROWN, individually and in his official capacity,

Respondents.

Petition For A Writ Of Certiorari
To the United States Court Of
Appeals For The Sixth Circuit

PETITION FOR WRIT OF CERTIORARI
with appendix

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51 pp

QUESTIONS PRESENTED FOR REVIEW

1. Whether denying an individual a government/state backed loan, solely because that individual has received a discharge, violates 11 U.S.C.A. §525.

2. Is 11 U.S.C. 106 constitutional, in that it purports to abrogate sovereign immunity?

PARTIES TO THE PROCEEDINGS

The petitioner is Sue Toth, an individual.

The respondent, Michigan State Housing Development Authority, is a governmental agency;

The respondent, James Logue, is an individual, and an official of Michigan State Housing Authority;

The respondent, Robert Brown, is an individual and an official of Michigan Housing Development Authority.

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MICHIGAN STATE HOUSING DEVELOPMENT AUTHORITY, in their official capacity; JAMES LOGUE III individually and in his official capacity; ROBERT BROWN, individually and in his official capacity,

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PETITION FOR WRIT OF CERTIORARI

Sue Toth respectfully asks that a writ of certeorari issue to review the judgment of the United States Court of Appeals for the Sixth Circuit in this case.

OPINIONS BELOW

The opinion on the Court of appeals, review of which is sought, is recommended for full text publication pursuant to Sixth circuit Rule 24 and is reproduced in the Appendix attached to this Petition at **App. A.** The opinion of the District Court is reproduced in the Appendix attached to this Petition at **App. B**.

STATEMENT OF JURISDICTION

BASIS FOR JURISDICTION IN THE COURT IN THE COURT OF FIRST INSTANCE

This action was brought pursuant to 42 U.S.C. § 1983, 11 U.S.C. §525, the fifth, and fourteenth amendment to the United States Constitution. Jurisdiction is founded upon 28 U.S.C. sections 1331, 1334, 1343(3), and 1471 and (4) and the aforesaid statutory and constitutional provisions and under U.S.C.A. Constitutional article 3 § 1 et seq.

JURISDICTION FOR SUPREME COURT

The decision of the Court of Appeals was entered on February 12, 1998. The Court has jurisdiction pursuant to 28 U.S.C. §1254(1).

STATEMENT OF THE CASE

Plaintiff received a discharge in bankruptcy on June of 1995. Several months later, she applied to the Michigan State Housing Development Authority ("MSHDA") for a home improvement loan. That agency administers a home improvement loan program of the United States Department of Housing and Urban Development designed to assist eligible low income participants. Thereafter, in November

1995, MSHDA notified plaintiff that her loan application had been denied due to the agency's policy of requiring at least three years after the date of a bankruptcy before a loan application will be processed.

ARGUMENT WITH RESPECT TO DISCRIMINATION UNDER 11 U.S.C. §525

REASONS FOR GRANTING THE WRIT

Certiorari is appropriate in this case under Sup. Ct. Rule 10.1(a) and 10.1(b). The Sixth Circuit has decided an important question of federal law that has not been, but should be, settled in this court. In particular, the Sixth Circuit decided 11 U.S.C. 525 (a) does not include within its purview either the extension of credit by home loan programs backed by governmental agencies. This decision conflicts with the intent of Congress to establish clear, consistent and enforceable standards to eliminate discrimination against individuals who have filed for protection under the bankruptcy laws of the United States. The Sixth Circuit decision also conflicts with other courts of appeals, BAP, and bankruptcy decisions, which have found that discrimination on extensions of credit by home loan programs of the nature involved violates 11 U.S.C. 525.

Additionally, the Sixth Circuit sidestepped an important issue that desperately needs to be settled in this court; that issue being whether 11 U.S.C. §106 meets constitutional muster.

A. The Court of Appeals' Decision Conflicts with the Intent of Congress and the Purpose of 11 U.S.C. § 525.

The Congressional intent appears clear by a cursory reading of the Legislative history of 11 U.S.C. § 525, wherein it states: "The enumerations of various forms of discrimination against former bankrupts is not intended to permit other forms of discrimination. The Courts have been developing the *Perez* rule . . . This section permits further development to prohibit actions by governmental or quasi governmental organizations . . .or by other organizations that can seriously affect the debtor's livelihood or fresh start . . . ."

Question? Is that too much for a provider of credit by a state entity to ask what caused the bankruptcy, or why the individual debtor filed for bankruptcy--giving the individual a chance to explain the circumstances that lead to their bankruptcy. Or maybe the provider might ask other pertinent questions such as (as illustrated in the Legislative History) . . . How secure is your employment . . . What is your income in relation to the anticipated payments . . . What is your security for the loan . . . Have you reestablished your credit and with whom . . . Do you think you could get a co-signer? Upon the reading of legislative history it would appear that is what is intended, so that the determination of credit worthiness is not based **solely** upon the filing of a bankruptcy (which in and of itself is not determinative of credit worthiness–the filing of a bankruptcy can be for reasons other than debt–such as to

quash a frivolous lawsuit). Therefore, if there is a bona fide nondiscriminatory examination of future financial responsibility in a particular lending practice,§525 does not come in to play. The relevant part of the legislative history states as follows: "It does not prohibit consideration of other factors, such as future financial responsibility or ability, and does not prohibit imposition of requirements such as net capital rules, if applied nondiscriminatorily." Even the V.A. Pamphlet 26-7 Change 15 dated April 12, 1994 , under the subtitle Bankruptcy, states as follows:

> "Credit information that shows the borrower or spouse has been adjudicated bankrupt under the straight liquidation and discharge provisions of bankruptcy law ***does not in itself disqualify the loan***. However, in such cases, it is necessary to develop complete information on the facts and circumstances of the bankruptcy. . ." (Emphasis added). (R 11 Exhibit "A"); JA pg. ___.

This reasoning would harmonize with the legislative history of 11 U.S.C.A. § 525.

In the case at bar, the debtor was employed by myself, her home was paid for, her payments would have been under $90.00 per month and she had no other debts. The reason for her bankruptcy was that her husband deserted her and their child, without explanation, or warning. Her husband left her with all the bills and without a source of income to pay those bills. She filed for divorce, Pro Se, (her

ex-husband was ordered to pay child support but as his whereabouts are unknown, he therefore does not pay child support) sought employment and attempted to repay the family debts. At minimum wage the task was impossible, and she filed for protection by filing for bankruptcy. The final irony was that after being denied her state backed MSHDA loan she was approved, by the same lender handling the MSHDA loan, for a standard conventional loan, and applied and received a loan for the purchase of an automobile. Apparently the conventional lender did not discriminate solely due to her prior bankruptcy, but looked beyond the bankruptcy and used other factors to determine her creditworthiness i.e. equity in secured property, reason for the bankruptcy, income to debt ratio, stability of employment and income, and after review of the information, made a determination that the debtor was credit worthy.

The holdings in the courts below reason that if Congress meant that discrimination against lending was not prohibited than Congress would have stated that in the body of the statute. That opinion flies squarely in the face of the legislative history where it states: "In addition, the section in not exhaustive. The enumeration of various forms of discrimination against former bankrupts ***is not intended to permit other forms of discrimination***." (emphasis added). Additionally, it goes on to say: "It does not prohibit consideration of other factors, such as future financial responsibility or ability, and does not prohibit imposition of requirements such as net capital rules, if applied

nondiscriminatorily." The above language clearly is indicative and relates to lending or the extensions of credit. Why would Congress give examples of other factors--relating to extension of credit--if extensions of credit was not implied as one of the enumerations not listed. The appellate court below skirted around this fact when they stated in their opinion: "The items enumerated in the statute -- licenses, permits, charters, and franchises -- are benefits conferred by government that are unrelated to the extension of credit." I find it odd that the word grant was omitted in the above discussion. Yet the court readily admit that "One could, of course, argue that the scope of § 525(a)'s `other similar grant' language should be construed broadly . . ." The court decides for a narrow interpretation of the statute. The legislative history suggests that this section be interpreted broadly. Collier on Bankruptcy ¶ 525.02[5] Rev.60–12/96 Pub219. Is not the granting of a franchise usually subject, in most cases, to having the proper financing or capital investments and does the government grant the franchises? Is not the same true with the issuing of a grant. How is that different than a governmental backed loan program?

Exhaustive according to Websters definition of exhaustive is leaving nothing out; covering every detail. Considering the negative of the word exhaustive -- not exhaustive would mean that the legislature did cover every detail when passing 11 U.S.C.A. § 525.

Consider the many reasons that debtors file for bankruptcy . . .illness--loss of employment--disability--death. Consider the following examples: 1. A mother and father

had a sixteen year old daughter. Their daughter had problems breathing. The parents brought their daughter in for medical evaluations. Nothing was found as a reason for their daughter's problems and the parents continued their search for an answer. After several years and thousands of dollars in medical it was discovered that their daughter had a terminal lung disease and she died. The girls parents did not even have the funds to give their daughter a proper burial. The mother was working for $5.15 an hour and the father was on social security. Their combined income was $1,200.00 per month. It would have been impossible to repay the hundreds of thousands of dollars in medical bills. 2. An individual is the sole shareholder in his corporation and is the key person in the corporation. He is involved in an auto accident in which he was a passenger, the accident was through no fault of him nor the driver of the vehicle -- the debtor was disabled and unable to continue his duties in the corporation and the corporation failed, leaving him in debt beyond his ability to resolve. In the case of Ms. Toth -- her husband, the sole provider, decided to abandon his wife and child. Left without a goodby and without letting anyone know his whereabouts. The only thing he did not take with him was the debt. He left his wife and child with no money or means of support. I think we all would agree that there are numerous examples such as these that could be told where the bankruptcy is beyond the control of the debtors. But the question remains -- should these individuals be discriminated against **solely** because they took advantage of the fresh start guaranteed under the bankruptcy laws of the

United States. If the answer is yes than my argument fails, and America is not what it claims to be.

B. The Decision Below Conflicts with Decisions in other Courts.

It is peculiar that 68 A.L.R. Fed. 128 and 137 (incorporated into this argument by this reference) and Collier on Bankruptcy, 525.05 (Rel 55-8/95 Pub) (also incorporated into this argument by this reference), both support the assumption that denying a debtor a governmental backed loan solely because of a prior bankruptcy violates 11 U.S.C.A. 525(a) of the Bankruptcy Code. It is conceded that the above authorities do not make the final determination of what the law is, that is left up to ultimate interprers of the law -- The Supreme Court of the United States.

The argument in support of prohibiting discrimination as stated in Collier's on Bankruptcy is paraphrased as follows:

It is sometimes not clear whether a particular government program or benefit falls within the scope of the phrase "license, permit, charter, franchise, or other similar grant." While this language clearly includes such things as driver's licenses and other licenses, its outer limits are less well-defined. The legislative history suggests that this section be interpreted broadly.

Courts have had little trouble finding a variety of governmental subsidy programs to be within this language. A public housing tenant may not be denied the continued

right to live in his or her apartment, and thus denied the subsidy inherent in public housing, because of unpaid rent which is discharged or dischargeable or because a bankruptcy has been filed, even if the bankruptcy has the effect of causing rejection of the preexisting lease. In re Curry, 148 B.R. 966 (S.D. Fla. 1992); Gibbs v. Housing Auth.of City of New Haven, 76 B.R. 257 (D. Conn. 1983); In re Szymecki, 87 B.R. 14 (Bankr.W.D. Pa. 1988); In re Sudier, 71 B.R. 780 (Bankr. E.D. Pa. 1987). A state program offering mortgage assistance cannot deny 'benefits based upon the filing of bankruptcy or upon the automatic stay provided by a bankruptcy filing. Rose v. Connecticut Hous. Fin. Auth. (In re Rose), 7 C.B.C.2d 909, 23 B.R. 662 (Bankr. D. Conn. 1982); but see Watts v. Pennsylvania Hous. Fin. Agency, 876 F.2d 1090, 21 C.B.C.2d 521 (3d Cir. 1989) (state mortgage assistance program involved loans rather than grants and was therefore outside scope of section 525).

The Court of Appeals for the Fifth Circuit, in Exquisi to Services, Inc. v. U. S.A., (In re Exquisi to Servs., Inc.), 823 F.2d 151, 154, 17 C.B.C.2d 324, 328 (5th Cir. 1987). held that participation in a Small Business Administration Program under which a debtor receives various types of assistance constitutes a franchise. The court adopted the definition of "franchise" in Black's Law Dictionary as a special privilege conferred by government on an individual or corporation, which does not belong to citizens generally of common right. That same source defines "license" as the authority or liberty given to do or forbear any act, or the

permission by some competent authority to do some act which, without such permission, would be illegal. Black's Law Dictionary 658 (6th ed. 1990).

Section 525(a) is applicable to a variety of other benefits, privileges, and services as well. The right to conduct business operations may not be conditioned on payment of prepetition premiums due to a state workers' compensation fund. In re Geffken, 11 C.B.C.2d 1223, 43 B.R. 697 (Bankr. N.D. Ohiol984). Permission to be a self-insurer under workers' compensation laws may not be denied solely because of a bankruptcy filing. In re Rath Packing Co., 9 C.B.C.2d 1295, 35 B.R. 615 (Bankr. D.lowa 1983); In re Hillcrest Foods, 10 B.R. 579 (Bankr. D. Me. 1981). Schools that are governmental units are not permitted to deny students the right to receive their transcripts based upon dischargeable debts for tuition or student loans. Lee v. Board of Higher Educ. of the City of New York, 1 B.R. 781 (S.D.N.Y. 1979); In re Dembek, 15 C.B.C.2d 611, 64 B.R. 745 (Bankr. N.D. Ohio 1986); Board of Trustees of the Univ. of Ala. v. Howren (In re Howren), 4 C.B.C.2d 153, 10 B.R.303 (Bankr. D. Kan. 1980); In the Matter of Heath, 1 C.B.C.2d 736, 3 B.R. 351 (Bankr. N.D. Ill.1980).

Notwithstanding the legislative history, some courts have read the language of section 525 more narrowly. The Court of Appeals for the Second Circuit has held that the right to have the state guarantee a' student loan was not within its scope because section 525 was not intended to reach decisions regarding the extension of credit. In re Goldrich, 771 F. 2d 28, 13 C.B.C.2d 468 (2d Cir. 1985).

Contra In re Richardson, 5 C.B.C.2d 429, 15 B.R. 925 (Bankr. E.D. Pa. 1981), rev'd on other grounds, 8 C.B.C.2d 79, 27 B.R. 560 (E.D. Pa. 1982). Similarly, the Court of Appeals for the Third Circuit has held that a state subsidized mortgage assistance program, in which the applicant agrees to repay the assistance on a deferred basis at below-market interest, is an extension of credit outside the scope of section 525. Watts v. Pennsylvania Hous. Fin. Agency, 876 F.2d 1090, 21 C.B.C.2d 521(3d Cir. 1989). While the conclusion that section 525 does not apply to extensions of credit may be generally correct, the courts did not adequately consider whether the state programs involved were in fact more in the nature of benefits conferred upon needy applicants, without regard to their credit worthiness, and therefore more similar to a franchise or similar grant, rather than an extension of credit. It is one thing to construe the legislative history narrowly; it is quite another to render it virtually meaningless. When Congress stated "The enumeration of various forms of discrimination against former bankrupts is not intended to permit other forms of discrimination,." this would imply a broad interpretation, it appears that some courts render the legislative history meaningless when they hold in their opinions that if congress mean it they would said it.

The decision of the Court of Appeals for the Second Circuit in In re Goldrich, 771 F.2d 28, 13 C.B.C.2d 468 (2d Cir. 1985), with respect to student loans was specifically overruled by Congress when it enacted section 525(c) as part of the Bankruptcy Reform Act of 1994. Pub. L. No. 103-394

(enacted on October 22, 1994, and effective with respect to cases filed on or after that date). In the legislative history of that section, the House Judiciary Committee stated that the court in that case had given "an unduly narrow interpretation to Code section 525." 140 Cong. Rec. HIO,771 (daily ed. Oct. 4, 1994) (remarks of Rep. Jack Brooks), reprinted in App. Pt. 9(b) infra; H.R. Rep. No. 835, 103d Cong., 2d Sess. 58 (1994). Thus, not only decisions permitting discrimination with respect to student loans, but also decisions permitting discrimination in other loan-related benefit programs, must be questioned anew in light of this clear statement of Congressional intent. The reference in section 525(c) to cases filed under the Bankruptcy Act, as well as to those filed under the Code, strongly bolsters the argument that Congress intended the amendment to clarify existing law applicable to past and pending cases as well as to cases filed after its enactment.

ARGUMENT WITH RESPECT TO 11 U.S.C. §106

A. Section 11 U.S.C. §106 is constitutional because it does not compel states to submit to the jurisdiction of a federal forum.

Judge Francis G. Conrad (Bankr. D. Vt.) Ruled in Francis O'Brien v. State of Vermont (In re Francis O'Brien), No. 95-10946 FGC, Adv. No. 96-104 (Feb. 2, 1998), that Contrary to some courts' readings of *Seminole Tribe of*

Florida v. Florida, Section 106 is constitutional because it does not compel states to submit to the jurisdiction of a federal forum. Rather, it requires, when personal jurisdiction over the state is necessary to determine the issues, that the bankruptcy court defer to the state's election not to have its rights adjudicated in a federal forum.

B. Section 11 U.S.C. §106 is constitutional because Congress acted under a valid exercise of power granted by the Constitution of the United States.

i. Article I Section 8 of the United States Constitution states: "To establish an uniform rule of Naturalization, and uniform Laws on the subject of Bankruptcies throughout the United States. The passing of the 11th Amendment to the United States Constitutional was not intended to strip away the intent of Article I Section 8 of the Constitution.

ii The 11th Amendment to the Constitution is not ambagious and should be read literally.

The 11th Amendment states: "The Judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by Citizens of another state, or by Citizens of Subjects of any Foreign State."

The Eleventh Amendment does not purport to overrule the principle on which *Chisolm v. Georgia* was based, i.e. sovereignty of the people, embodied in their National government, and for national purposes superior to the sovereignty of the States. In Re Southern Star Foods, Inc. 190 B.R. 419 (Bkrtcy. E.D. Okl. 1995). By its express terms, the Eleventh Amendment to the United States Constitution immunizes a State from suit in the federal courts by a non resident of that State. In re Straight, 209 B.R. 540 (D. Wyo. 1997)

iii. Congress has the power to pass §106 pursuant to the Fourteenth Amendment.

The 14th Amendment provides that citizens of the United States may rely upon their national Congress to enforce their national rights against the States. Id.

Additionally, MSHDA consented to the excercise of jurisdiction by a magistrate judge who issued the district court's opinion . . . .Toth v. Mich. State Housing Develop. Auth., 1998 U.S. App. Lexis 1939, 1998 FED. App. 0053P

The Decision Below Conflicts with Decisions in other Courts.

In a non-bankruptcy case, Seminole Tribe of Florida v. Florida, 116 S. Ct 114 (1996), the majority or the Supreme Court held that Congress lacks power to subject a state to suit

in federal court except when it legislates pursuant to the specific authority of the Enforcement Clause of the Fourteenth Amendment.

Since the above decision the lower courts have been struggling trying to resolve how the case pertains to bankruptcy law. The first case involving bankruptcy with regard to 11 U.S.C. §106, In the Matter of MERCHANTS GRAIN, INC. 59 F. 3rd 630 (7th Cir. 1995), the Supreme Court remanded the case for further consideration in light of the Seminole case. 116 S. Ct. 1411, 134 L.Ed. 2d 537, 64 USLW 3682, 64 USLW 3689.

Thereafter cases involving the same issue have been oscillating back and forth from holding the statute constitutional to holding the statute unconstitutional.

The case of In re Straight, 209 B.R. 540 (D Wyo. 1997, Johnson, D.J.) the court held that the Seminole Tribe, decision did not invalidate § 106(a) as it applies to states. Abrogation of a state's sovereign immunity as provided in § 106(a) is a valid exercise of Congress' power under section 5 of the Fourteenth Amendment to endorse the privileges and immunities of citizens of the United States (as conferred by the Bankruptcy Code) by creating private rights of action against states. (The opinion follows the analysis of In re Southern Star Foods Inc., 190 B.R. 419 (Bankr. E.D. Okla. 1995), and In re Headrick, 200 B.R. 963 (Bankr. S.D. Ga. 1996).

The case of In re NVR L.P., 206 B.R. 831 (E.D. Va. 1997, Tice, B.J.) the court held that state's sovereign immunity as enunciated in the Seminole decision applies

even in a declaratory relief proceeding against the state. The state's filing of a proof of claim does not constitute a wholesale submission to the jurisdiction of the bankruptcy court. At most, such filing is only a consent to the adjudication of that claim. Section 106(b) is unconstitutional to the extent it purports to provide for a broader waiver of sovereign immunity.

The case of In re Paul's Lobster Co., Inc., 206 B.R. 275 (D. Mass. 1997, Kenner, B.J.) the court held that the debtor's action against the Commonwealth based on a constructive taking of property was barred in the bankruptcy court by an assertion of sovereign immunity. Even if Congress could constitutionally abrogate a state's sovereign immunity, the provisions of § 106(a) would not apply to this kind of cause of action.

In the case of In re Burke, 203 B.R. 493, 30 BCD 62 (S.D. Ga.1996, Dalis, B.J.), the court held that Section 106(a), which abrogates state sovereign immunity, is a constitutional exercise of Congress' power under the privileges and immunities clause of the Fourteenth Amendment *Seminole Tribe* does not compel a contrary conclusion.

The case of In re Tri-City Turf Club, Inc., 204 B.R. 617, 30 BCD 81 (E.D. Ky. 1996, Howard, B.J.) stated that there in no indication that Congress had the Fourteenth Amendment in mind when it enacted § 106(a).

The case of In re Lush Lawns, Inc. 203 B.R. 418, 29 BCD 1311 (N.D. Ohio 1996, Baxter, B.J.), held under *Seminole Tribe*, the bankruptcy court lacks jurisdiction to

impose sanctions or contempt penalties against a state that has violated the automatic stay.

Also, the case of Natural Resources Defense Counsel v. California Dept. of Transp. 96 F.3rd 420 (9th Cir. 1996) held that the lower court did not violate the Eleventh Amendment as construed in the *Seminole Tribe* decision, 116 S. Ct. 1114 (1996). [See also In re National Cattle Congress, Inc., 91 F.3d 1113 (8th Cir. 1996) (raising issue of whether Eleventh Amendment precluded enforcing automatic stay against the state's revocation of the debtor's dog racing licence). Matter of Midland Mechanical Contractors, Inc., 200 B.R. 453, 29 BCD 933 (N.D. Ga. 1996, Drake B.J.) (under *Seminole Tribe*, court lacked subject matter jurisdiction over suit against state agency). In re Hanover-York Development, Inc., 201 B.R. 137, 29 BCD 1066 (E.D. N. Car. 1996, Small, B.J.) (Eleventh Amendment as construed in *Seminole Tribe* precludes application of § 106(a) to states.]

In re HPA Associates, 191 B.R. 167, 28 BCD 547 (9th Cir. BAP 1995) held that the 1994 amendment to § 106(a), which abrogates a state's Eleventh Amendment sovereign immunity with respect to various specified sections of the bankruptcy Code, is a constitutional exercise of the Congress' Article I bankruptcy power. (The opinion cites the various judicial authorities that support this conclusion but also refers to the considerable present uncertainty concerning the law on this issue).

Recently, Judge John E. Ryan (Bankr. C.D. Cal.), ruled in Gregory R. and Carol H. Morrell v. Franchise Tax

Board (In re Gregory R. and Carol H. Morrell), No. SA 97-11910 JR, Adv. No SA 97-1527 JR (Dec. 19, 1997) that Sovereign immunity prevents bankruptcy courts from determining the dischargeability of state tax liens. In reaching this conclusion, the court agreed with those decisions that found section 106(a) unconstitutional in light of the Supreme Court's Seminole decision.

CONCLUSION

For the reasons set forth herein, the Court's standards for granting certiorari, as set for in Sup. Ct. Rule 10.1, are well met in this case. Consequently, the petitioner respectfully submits that the petition should be granted.

Respectfully sumitted,

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APPENDIX A

UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF MICHIGAN
NORTHERN DIVISION

SUE TOTH,

Plaintiff,

V.

Case No. 2:96-cv-018
CONSENT CASE

MICHIGAN STATE HOUSING
DEVELOPMENT AUTHORITY, et al.,

Defendants.

OPINION

I. FACTS

Plaintiff Sue Toth filed this 42 U.S.C. 9 1983 action against defendant Michigan State Housing Development Authority (MSHDA), and also named defendants MSHDA employee James L. Logue III and MSHDA agent Robert Brown in their official and individual capacities. on June 1, 1995 Sue Toth received a discharge in bankruptcy from this court. Sue Toth, subsequently applied for a low income MSHDA home improvement loan at the Northern Michigan Bank in Kingsford, Michigan. Ms. Toth was informed that her loan application was rejected in accordance with MSHDA policies which required three years from the discharge of a bankruptcy before a loan application will be processed. Ms. Toth was forced to apply for a loan at

the prevailing market rate. Plaintiff alleges that she was discriminated against in violation of 11 U.S.C.§ 525 of the Bankruptcy Code and contrary to Perez v. Campbell, 402 U.S. 637(1971), and in violation of the Fifth and Fourteenth Amendments.

II. MOTION STANDARD

Plaintiff filed a Fed. R. Civ. P. 12 motion for judgment on the pleadings or alternatively under Rule 56 for summary judgment. Defendants filed a motion for summary judgment. Since matters outside the pleadings have been presented by the parties the court will treat the motions as arising under Rule 56. Summary judgment is appropriate only if the moving party establishes that there is no genuine issue of material fact for trial and that he is entitled to judgment as a matter of law. Fed. R. Civ. P. 56(c); Celotex Corp. v. Catrett, 477 U.S. 317, 322-323 (1986). If the movant carries the burden of showing there is an absence of evidence to support a claim or defense, then the respondent must demonstrate by affidavits, depositions, answers to interrogatories, and admissions on file, that there is a genuine issue of material fact for trial. Id. at 324-25. The respondent cannot rest on its pleadings but must present "specific facts showing that there is a genuine issue for trial." Id. at 324 (quoting Fed. R. Civ. P.56(e)). While the evidence must be viewed in the light most

favorable to the nonmoving party, a mere scintilla of evidence in support of the nonmovant's position will be insufficient. Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 251-52 (1986). Ultimately, the court must determine whether there is sufficient "evidence on which the jury could reasonably find for the plaintiff.,,Id. at252. See also Leahy v. Trans Jones, Inc., 996 F.2d 136, 139 (6th Cir. 1993) (single affidavit, in presence of other evidence to the contrary, failed to present genuine issue of fact) ; cf. Moore, Owen, Thomas & Co. v. Coffey, 992 F.2d 1439, 1448 (6th Cir. 1993) (single affidavit concerning state of mind created factual issue)

III. ANALYSIS

A. ELEVENTH AMENDMENT

Defendants assert that the Eleventh Amendment bars a suit against the state. Seminole Tribe of Florida v. Florida, 517 U.S. -, 116 S.Ct. 1114 (1996). It is clear that 11 U.S.C.106(a) clearly abrogates a states sovereign immunity when the state is sued under 11 U.S.C. 525 for non-punitive damages. Defendants are entitled to dismissal under this theory of only plaintiff's claims for punitive damages.

B. 42 U.S.C. S 1983

Plaintiff brings this suit under 42 U.S.C.1983. MSHDA and the individual

defendants in their official capacity argue that

they are not persons under Section 1983. Will v. Michigan Dept. of State Police, 491 U.S. 58 (1989). Under Will, a suit against a state, a state agency or a state official in his official capacity is not a suit against a "person" under Section 1983. Id Thus, such entities are not subject to suit under 42 U.S.C.§ 1983. In re Saunders, 105 B.R. 781, 785 (E.D. Penn. 1989) Accordingly, plaintiff's Section 1983 action is dismissed against MSHDA and the individual defendants in their official capacity.

C. **BANKRUPTCY DISCRIMINATION**

Plaintiff alleges that under 11 U.S.C. § 525 she was unlawfully discriminated against because her loan application was denied solely because of her discharge in bankruptcy. Section 525 states in applicable part:

> (a) .... a governmental unit may not deny, revoke, suspend, or refuse to renew a license, permit, charter, franchise, or other similar grant to, condition such a grant to, discriminate with respect to such a grant against, deny employment to, terminate the employment of, or discriminate with respect to employment against, a person that is or has been a debtor under this title or a bankrupt or a debtor under the Bankruptcy Act, or another person

> with whom such bankrupt or debtor has been associated, solely because such bankrupt or debtor is or has been a debtor under this title or a bankrupt or debtor under the Bankruptcy Act, has been insolvent before the commencement of the case under this title, or during the case but before the debtor is granted or denied a discharge, or has not paid a debt that is dischargeable in the case under this title or that was discharged under the Bankruptcy Act.

Congress enacted this section to codify the decision in Perez v. Campbell, 402 U.S. 637 (1971). In Perez, the Arizona Highway Department refused to renew the drivers license of an individual who had a judgment discharged in a bankruptcy proceeding. The Arizona statute provided for the suspension of a license of any driver who failed to pay an outstanding automobile accident judgment. The Supreme Court struck down the Arizona statute as a violation of the Supremacy Clause. The purpose behind the statute is to prevent governmental units from frustrating the policies of the Bankruptcy Code by discriminating against individuals who have filed for bankruptcy protection. Duffy v. Dollison, 734 F.2d 265,271 (6th Cir. 1984).

The issue presented in this case is whether the denial of a MSHDA home loan solely because the applicant had filed a bankruptcy within three years of the loan

application violated Section 525. It appears that the Sixth Circuit has not decided this issue. The parties concede that there is a split of authority among those courts who have decided this issue. Courts that have determined that the denial of a loan based on a previous bankruptcy violates the Act include Rose v. Connecticut Housing Finance Authority, 23 B.R. 662 (D. Conn. 1982) (denial of home loan based on bankruptcy discharge of student loan), and In re Richardson, 27 B.R. 560 (E.D. Penn 1982) (denial of student loan based on previous discharge in bankruptcy of student loans). It appears that the rationale these courts used to extend Section 525 to loans was based on courts' broad application of Section 525 and the fact that a governmental unit was involved in the financing. Rose, at 666.

Courts that have held that Section 525 is not applicable to a loan include In re Cleasby, 139 B.R. 897 (W.D. Wis. 1992)(Farmers Home Administration denial of debt restructuring), Watts v. Pennsylvania Housing Finance Co., 876 F.2d 1090 (3d Cir. 1989)(Denial by Pennsylvania Housing Finance Agency of continued access to mortgage loan guarantee program), and In re Goldrich, 771 F.2d 28 (2d Cir. 1985) (denial of student loan based on previous discharge of student loan in bankruptcy). The rationale these courts follow in refusing to apply Section 525 broadly to credit applications and loans is that they are distinct from the type of protection the Act intended to cover. A loan

is not a license, permit, charter, franchise or other similar grant. Moreover, these courts concluded that the omission of post bankruptcy credit arrangements from Section 525 was intentional. If Congress intended that Section 525 cover loans and credit it could have included some language to support such an extension. In re Cleasby, at 900.

I agree with the Fifth Circuit which cautions that the better approach to take when analyzing the statute is to narrowly construe the statute. In re Exquisito Services, Inc., 823 F. 2d151, 152 (5th Cir. 1987). Clearly, it appears that Section 525 was not intended to cover post bankruptcy home improvement loans. Such a loan is not a license, permit, charter or franchise or in any way similar to those grants. I am unwilling to extend the language of the Act to cover post bankruptcy loans. In making this conclusion I recognize that Congress intended for the courts to develop the scope of Section 525 within the confines of sound bankruptcy policy. In re Rees, 61 B.R. 114, 119-120 (D. Utah 1986), In re Exquisito Services, Inc., at 152.

Plaintiff argues in her brief that any time a governmental unit discriminates against an individual on the basis of a prior bankruptcy, Section 525 is violated. Such a broad reading of Section 525 is not appropriate. If Congress intended Section 525 to cover every potential form of

discrimination, Section 525 would not contain the limiting language that it is applicable only to-,a license, permit, charter, franchise, or other similar grant . . . . " Congress could have simply used language stating that a governmental unit may not discriminate on the basis of a prior discharge in bankruptcy without inclusion of any limiting language or specific areas of concern. Moreover, if Congress intended Section 525 to apply to all post bankruptcy loans, Congress could have simply added all loans to the statute. Congress chose not to make such an addition. In 1994 the statute was amended to include student loans. The statute states:

> (c)(1) A governmental unit that operates a student grant or loan program and a person engaged in a business that includes the making of loans guaranteed or insured under a student loan program may not deny a grant, loan, loan guarantee, or loan insurance to a person that is or has been a debtor under this title or a bankrupt or debtor under the Bankruptcy Act....or has not paid a debt that is dischargeable in the case under this title or that was discharged under the Bankruptcy Act.

The amendment clearly does not cover all types of loans but only student loans. The exclusion of home improvement loans in

this amendment establishes that Congress did not intend that Section 525 extend to these types of loans.

D. **QUALIFIED IMMUNITY**

Defendants James L. Logue III and Robert Brown are entitled to qualified immunity from damages when sued in their individual capacity. Government officials, performing discretionary functions, generally are shielded from liability for civil damages insofar as their conduct does not violate clearly established statutory or constitutional rights of which a reasonable person would have known. Harlow v. Fitzgerald, 457 U.S.800, 818 (1982). An "objective reasonableness" test is used to determine whether the official could reasonably have believed his conduct was lawful. Anderson v. Creighton, 483 U.S. 635, 641(1987) . That is, in light of pre-existing law, the unlawfulness of the officials conduct must be apparent. Wegener v. City of Covington, 933 F.2d 390, 392 (6th Cir. 1991).

The operation of the qualif ied immunity standard depends substantially upon the level of generality at which the relevant legal rule is to be identified.

> The contours of the right must be sufficiently clear that a reasonable official would understand that what he is doing violates that right. This is

> not to say that an official action is protected by qualified immunity unless the very action in question has previously been held unlawful, but it is to say that in light of the preexisting law the unlawfulness must be apparent.

Anderson, 483 U.S. at 639-40.

Thus, qualified immunity is not triggered only where the very action in question was previously held unlawful. Id. at 639-40. Rather, the test is whether the contours of the right were sufficiently clear that a reasonable official would understand that what he is doing violated plaintiff's federal rights. id. When faced with a qualified immunity defense, the court must first determine whether or not the plaintiff has stated a claim upon which relief can be granted. Siegert v. Gilley, 500 U.S. 226 (1991). If the court answers that question in the affirmative, the court goes on to determine whether or not the right allegedly violated was clearly established. These are both purely legal questions.

For the reasons previously stated, plaintiff has failed to state a claim against the defendants. Accordingly, the individual defendants are entitled to qualified immunity. Moreover, as both parties concede, the Sixth Circuit has not decided this issue and there is a split of authority among the courts which have decided this issue. There

was no clearly established law prohibiting defendants from denying the loan application based on the past discharge in bankruptcy. Moreover, there clearly existed authority providing that the action that defendants took was lawful. Since no clearly established law could possibly have been violated by the individual defendant's actions,these defendants are also entitled to qualified immunity.

IV. CONCLUSION

Accordingly, defendants' motion for summary judgment will be granted, plaintiff's motion for judgment on the pleadings or alternatively motion for summary judgment will be denied, and this case will be dismissed in its entirety.

Dated: September,16 1996
TIMOTHY P. GREELEY UNITED STATES MAGISTRATE JUDGE

UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF MICHIGAN
NORTHERN DIVISION

SUE TOTH,
Plaintiff,

1. -

Case No.
2:96-cv-018
CONSENT CASE

MICHIGAN STATE HOUSING
DEVELOPMENT AUTHORITY, et al.,
Defendants.

JUDGMENT

In accordance with the Opinion issued herewith,

IT IS HEREBY ORDERED that defendants' motion for summary judgment (Docket #8) is granted, plaintiff's motion for judgment on the pleadings or alternatively motion for summary judgment (Docket#4) is denied, and this case is DISMISSED in its entirety. IT IS SO ORDERED.

Dated: September 1996
TIMOTHY P.GREELEY
UNITED STATES MAGISTRATE JUDGE

APPENDIX B

RECOMMENDED FOR FULL-TEXT PUBLICATION
Pursuant to Sixth Circuit Rule 24

ELECTRONIC CITATION: 1998 FED App.
0053P (6th Cir.)
File Name: 98a0053p.06

UNITED STATES COURT OF APPEALS

FOR THE SIXTH CIRCUIT

SUE TOTH,

Plaintiff-Appellant,

v.

MICHIGAN STATE HOUSING DEVELOPMENT AUTHORITY, in their official capacity; JAMES LOGUE III, individually and in his official capacity; ROBERT BROWN, individually and in his official capacity,

Defendants-Appellees.

> No. 96-2206

Appeal from the United States District Court
for the Western District of Michigan at Marquette.
No. 96-00018--Gordon J. Quist, District Judge.
Submitted: September 10, 1997
Decided and Filed: February 12, 1998

Before: MERRITT, JONES, and NORRIS, Circuit Judges.

COUNSEL

ON BRIEF: Allan J. Rittenhouse, Iron Mountain, Michigan, for Appellant. Steven D. Hughey, OFFICE OF THE ATTORNEY GENERAL, FINANCE & DEVELOPMENT DIVISION, Lansing, Michigan, for Appellees.

OPINION

ALAN E. NORRIS, Circuit Judge. Plaintiff Sue Toth appeals from the district court's grant of summary judgment to the Michigan State Housing Development Authority and two of its officers in an action alleging discrimination in violation of 11 U.S.C. § 525(a) of the Bankruptcy Code. She contends that the denial of her application for a low income home improvement loan based upon a recent discharge in bankruptcy was contrary to the language of § 525(a) of the Code. Plaintiff further claims that the violation of § 525(a) gives rise to a 42 U.S.C. § 1983 claim. Because we conclude that § 525(a) does not forbid consideration of a prior bankruptcy in post-discharge credit arrangements with state entities, we affirm.

I.

Plaintiff received a discharge in bankruptcy in June 1995. Several months later, she applied to the Michigan State Housing Development Authority ("MSHDA") for a home

improvement loan. That agency administers a home improvement loan program of the United States Department of Housing and Urban Development designed to assist eligible low income participants. Thereafter, in November 1995, MSHDA notified plaintiff that her loan application had been denied due to the agency's policy of requiring at least three years to lapse after the date of a bankruptcy discharge before a loan application will be processed.

Plaintiff filed suit in February 1996 in United States District Court for the Western District of Michigan alleging that MSHDA and two of its officials unlawfully discriminated against her in violation of § 525(a) of the Bankruptcy Code. She sued the two officials, James Logue III, executive director of MSHDA, and Robert Brown, manager of MSHDA's home improvement loan program, in both their official and individual capacities. Plaintiff contended that § 525(a) prohibits a state's denial of a low-interest home improvement loan based solely upon a prior discharge in bankruptcy, and that the violation of § 525(a) gave rise to a cause of action under 42 U.S.C § 1983.[1]

The parties consented to the exercise of jurisdiction by a magistrate judge, who issued the district court's opinion and order holding that the court had jurisdiction over the case

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[1] Although the complaint also purported to invoke the Fifth and Fourteenth Amendments to the United States Constitution, plaintiff failed to develop any theory under which any rights guaranteed by those provisions might have been violated.

notwithstanding the Eleventh Amendment,[2] and granted defendants' motion for summary judgment on the merits.

II.

The primary issue raised by this appeal is whether the denial by MSHDA of a home improvement loan solely because the applicant had been discharged in bankruptcy within three years of the loan application violates 11 U.S.C. § 525(a) of the Bankruptcy Code. Plaintiff asserts that the strictures of § 525(a) apply to the home improvement loan program operated by the Michigan agency to prohibit implementation of the agency's policy to deny her a loan based solely upon her prior discharge in bankruptcy. We disagree.

A.

Section 525(a) provides:

> (a) . . . a governmental unit may not deny, revoke, suspend, or refuse to renew a license, permit, charter, franchise, *or other similar grant to*, condition such a grant to, *discriminate with respect to such a grant* against, deny employment to, terminate the employment of, or discriminate with respect to employment against, a person that is or has been a debtor under this title or a bankrupt or a debtor under

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[2]The court below properly dismissed plaintiff's claims for punitive damages under § 106(a). Section 106(a) expressly abrogates a state's sovereign immunity from suit when the state is sued under § 525 for non-punitive damages. Thus, the Eleventh Amendment precludes plaintiff's claim against MSHDA for punitive damages.

> the Bankruptcy Act, or another person with whom such bankrupt or debtor has been associated, *solely because* such bankrupt or debtor is or has been a debtor under this title or a bankrupt or debtor under the Bankruptcy Act, has been insolvent before the commencement of the case under this title, or during the case but before the debtor is granted or denied a discharge, or has not paid a debt that is dischargeable in the case under this title or that was discharged under the Bankruptcy Act.

11 U.S.C. § 525(a) (1996) (emphasis added).

To the extent that it may apply to the circumstances of this case, § 525(a) prohibits a governmental entity from denying a "license, permit, charter, franchise, or other similar grant" or discriminating "with respect to such a grant" solely on the basis that the person seeking such a boon has been a bankrupt.

B.

One could, of course, argue that the scope of § 525(a)'s "other similar grant" language should be construed broadly, relying upon the general policy underlying bankruptcy, that a debtor should be able to have a "fresh start," to preclude conduct that would frustrate that policy. However, the courts of appeals that have approached the question have read the statute's reach narrowly, focusing upon the specific language of the statute. *See, e.g., Watts v. Pennsylvania Hous. Fin. Co.*, 876 F.2d 1090, 1093-94 (3d Cir. 1989); *In re Goldrich*, 771 F.2d 28, 30 (2d Cir. 1985). *Watts* involved an emergency

mortgage assistance program designed by the State of Pennsylvania to prevent imminent mortgage foreclosures by providing for loans to distressed borrowers in the form of direct payments to their mortgage lenders, keeping their mortgages current. When plaintiff borrowers filed for bankruptcy, the program suspended these payments for the duration of the Bankruptcy Code's automatic stay. Plaintiffs contended this suspension violated § 525(a). In response, the court of appeals noted that a loan from the Pennsylvania program simply was not a "license, permit, charter [or] franchise," and that since those terms "are in the nature of indicia of authority from a governmental unit to . . . pursue some endeavor," the term "similar grant" should be given the same meaning. *Watts*, 876 F.2d at 1093. Similarly, the court in *In re Goldrich* concluded that § 525(a) did not prohibit consideration of prior bankruptcies in credit decisions, since "the language of section 525 may not properly be stretched so far beyond its plain terms." *Goldrich*, 771 F.2d at 29. We agree with the analysis employed by our sister courts.

The items enumerated in the statute -- licenses, permits, charters, and franchises -- are benefits conferred by government that are unrelated to the extension of credit. They reveal that the target of § 525(a) is government's role as a gatekeeper in determining who may pursue certain livelihoods. It is directed at governmental entities that might be inclined to discriminate against former bankruptcy debtors in a manner that frustrates the "fresh start" policy of the Bankruptcy Code, by denying them permission to pursue certain occupations or endeavors. The intent of Congress incorporated into the plain language of

§ 525(a) should not be transformed by employing an expansive understanding of the "fresh start" policy to insulate a debtor from all adverse consequences of a bankruptcy filing or discharge. A reckoning of an applicant's financial responsibility is an essential part of any lender's evaluation of a post-discharge application for a loan or extension of credit.

Accordingly, the district court correctly concluded that plaintiff failed to make out a case of discrimination under § 525(a), since that section does not include within its purview either the extension of credit by home loan programs of the nature involved in this case, or the specific conduct of defendants about which plaintiff complains.

III.

Since violation of § 525(a) was the predicate for plaintiff's claim brought under 42 U.S.C. § 1983, no relief is available under § 1983.

IV.

The state defendants contend that the judgment in their favor can be affirmed on an alternative ground -- by reversing the district court's denial of their claim to sovereign immunity. This cross-assignment of error is based upon their reading of the Supreme Court's recent decision in *Seminole Tribe of Florida v. Florida*, 517 U.S. 44 (1996). Defendants contend that plaintiff's claims for money damages are barred by the State of Michigan's sovereign immunity as guaranteed by the Eleventh Amendment. We need not reach this contention. No notice of appeal was filed by these defendants, and their cross-

assignment of error must therefore be treated as having been raised only to protect the judgment below. In such an instance, error is assigned by an appellee only as a shield, cannot be used to modify the judgment, and will be considered only when necessary to prevent reversal of the judgment under review. *United States v. American Ry. Express Co.*, 265 U.S. 425, 435 (1924).

V.

The judgment of the district court is **affirmed**.